

Ex-Ante Evaluation (for Japanese ODA Loan)

Middle East Division 1, Middle East and Europe Department, JICA

1. Name of the Program

Country: Arab Republic of Egypt

Project: Development Policy Loan for Power Sector Reform

Loan Agreement: February 15, 2021

2. Background and Necessity of the Program

(1) Current State and Issues of the Economic and Power Sector in the Arab Republic of the Egypt and the Positioning of the Program.

The Arab Republic of Egypt (hereinafter referred to as “Egypt”) received a total of \$12 billion in loans from the International Monetary Fund (IMF) under their Extended Fund Facility over a period of three years from 2016, as well as financial support from the World Bank and other donors. They have used this funding for economic reforms such as reducing energy subsidies and introducing value-added tax. As a result, the country recorded a GDP growth rate of 5.6% in the 2018/2019 fiscal year, achieving fiscal consolidation, a reduction of account deficits, and an increase in foreign exchange reserves. Meanwhile, the spread of the novel coronavirus (hereinafter referred to as “COVID-19”) in 2020 has led to a decline in tourism revenue and workers’ remittances, which were Egypt’s main sources of earning foreign currency; the unemployment rate has also increased. In light of this, the Government of Egypt has been forced to take measures such as expanding assistance for the health sector and providing cash benefits to vulnerable citizens. Due to the higher government spending caused by these factors, the budget deficit (as a percentage of the GDP) was 8.0% in FY 2019/20 and is expected to widen to 8.4% in FY 2020/21 (IMF, 2020).

Egypt’s public finances are structured in such a way that current expenditure makes up most of its budget spending, with subsidies, government employee salaries, and debt interest payments accounting for more than half the total. In particular, subsidies account for more than 20% of total expenditure (FY 2018/19), with energy subsidies for electricity and fuel, etc., accounting for about 40% of the total subsidies (FY 2018/19). Although fuel subsidies were eliminated in July 2019, electricity subsidies are still in the process of being reduced. The electricity sector, including subsidy reduction, is in need of reform. Additionally, capital expenditure, which is an investment necessary for future economic development including the building of infrastructure, is only 2.7% of the GDP (IMF, 2019). In light of this situation, and while continuing to respond to the impact of COVID-19, the promotion of policy reforms, including increasing social capital investment and curbing current expenditure, such as subsidies, is a priority issue.

In February 2016, the Government of Egypt announced its long-term development strategy,

“Sustainable Development Strategy: Egypt Vision 2030” (hereinafter referred to as “Vision 2030”), and has made energy sector reform as a key policy measure. Specifically, the main actions include the formulation of a medium-to-long-term energy strategy, energy sector governance reform, and reducing energy subsidies for electricity and fuel.

In the power sector in particular, the stagnant financial condition of power utilities due to extremely low electricity tariffs and the growing size of government subsidies to compensate for this stagnation has been a longstanding problem, as have fiscal pressures and inflexible expenditures. The situation has also led to less incentive for power utilities to improve their management and organizational efficiency, and has caused a deterioration in governance. In addition, a self-sustaining and competitive electricity market in which the private sector can actively invest has not been created due to low electricity tariffs, which prevents proper cost recovery, and the lack of adequate public procurement rules and regulations. In order to enable a sustainable power supply, which is a key policy of Vision 2030, there is an urgent need to reduce power subsidies, which contribute to the power sector's budget deficit, improve the governance of power utilities, and increase private sector investment. The government is aiming to reduce electricity subsidies by raising the price of electricity in stages, increasing the rate by about 15% in 2019 and aiming to eliminate electricity subsidies by 2025 (subsidies for some of the poorest populations will continue). At the same time, the government is also working to advance governance reform in order to improve the financial situation and management efficiency of power utilities through this reduction of subsidies.

In addition, thermal power generation accounts for 91% of Egypt's power source mix (FY 2018/19), but the Government of Egypt has set a target to increase renewable energy power generation capacity from about 8% in FY 2017/18 to 20% by 2022, in order to diversify the power source mix from the perspective of green growth and energy security. With regard to energy efficiency, the Government of Egypt has released policy documents to promote energy conservation (such as the National Energy Efficiency Action Plan 2018-2022 (NEEAP II)), and is strengthening its structure for implementation within the government. They are also promoting efficiency in the power sector as a whole, including distribution companies and consumers.

Under these circumstances, the Development Policy Loan for Power Sector Reform (hereinafter referred to as the "Program") will support the Government of Egypt in further promoting structural reform of the power sector through financial assistance, with the aim of contributing to a sustainable and stable power supply, economic stability, and the promotion of development efforts.

(2) Japan and JICA's Policy in the Power Sector and Positioning of the Program

Japan's Country Assistance Policy for the Arab Republic of Egypt (June 2008) identifies the "realization of sustainable growth and employment creation" as one of its priority areas, and

Japan intends to support the Government of Egypt in their efforts on improving efficiency in energy use to meet the electricity demand, which is expected to increase along with population and economic growth in the future. In the JICA Country Analysis Paper for the Arab Republic of Egypt (March 2016) as well, the power sector has been identified as a priority area, aiming for inclusive and sustainable growth. In addition, in a joint statement issued at the Japan-Egypt Summit Meeting in 2016, the Japan-Egypt Joint Initiative for Cooperation in the Electricity Sector was announced. The Program is consistent with these policies and analyses, which state that improving capacity for supplying electricity and promoting its rational and efficient use are important for Egypt's sustainable development.

Through financial assistance, the Program will facilitate a sustainable and stable electricity supply, as well as economic stabilization in Egypt, thereby contributing to SDG 7 (securing clean and sustainable energy), SDG 8 (inclusive and sustainable economic growth), and SDG 13 (action to combat climate change). Furthermore, as support for the power sector, JICA is currently implementing the Power Sector Reform Advisor program (Individual Expert, 2018-2021), the Project for Capacity Development on Energy Efficiency and Conservation (Technical Cooperation, 2019-2021), and the Electricity Distribution System Improvement Project (ODA Loan, L/A signed in 2016).

(3) Other Donors' Activities

Through its Development Policy Financing, the World Development Bank implemented the Fiscal Consolidation, Sustainable Energy, and Competitiveness Programmatic Development Policy Financing Project in 2015 (US\$ 1 billion), 2016 (US\$ 1 billion), and 2017 (US\$ 1.15 billion). In addition, as a co-financing project with the World Bank, the African Development Bank (AfDB) implemented the Economic Governance and Energy Support Program in 2015 (\$500 million), 2016 (\$500 million), and 2018 (\$500 million), which focuses on fiscal consolidation, ensuring a sustainable energy supply, and improving the business environment.

3. Program Description

(1) Program Objectives

By supporting the implementation of reforms to address structural issues in the power sector through financial assistance, the Program aims to (1) strengthen financial sustainability and promote governance reforms in the power sector, and (2) promote renewable energy and energy efficiency for green growth, thereby contributing to a sustainable and stable power supply in Egypt and promoting economic stability and development efforts.

(2) Program Site/Target Area

The whole of the Arab Republic of Egypt

(3) Program Components

The AfDB, Agence Française de Développement (AFD), and JICA will work together to support the promotion of policy reforms based on the policy matrix that defines the reform objectives of the power sector, which consists of the following two policy areas and eight policy actions agreed upon by the Government of Egypt.

Policy area	Policy action
<u>Component 1</u> Strengthening of financial sustainability and promotion of governance reform in the power sector	(1) Gradual increase of electricity tariffs (2) Improvement of the financial condition of power-related organizations and power utilities (3) Expansion of private sector participation in the maintenance and management of power plants (4) Revision of public procurement rules for power utilities
<u>Component 2</u> Promotion of renewable energy and energy efficiency for green growth	(5) Expansion and promotion of small-scale solar power generation (6) Approval of policy documents related to energy efficiency (7) Strengthening the policy implementation structure for energy efficiency (8) Strengthening demand management by power distribution companies

(4) Estimated Program Cost

Loan amount: 25 billion yen

(5) Project Implementation Schedule

The signing of the L/A will signify the start of the Program's financial support. The target date for achieving the policy actions set as the requirements for the execution of the Program is April 2020. Since all policy actions have already been achieved, the Program will be considered finished upon disbursement of the loan, which will be done upon L/A signing and effectuation.

(6) Project Implementation Structure

- 1) Borrower: The Government of the Arab Republic of Egypt
- 2) Executing Agency: Ministry of Electricity and Renewable Energy

(7) Collaboration and Division of Roles with Other Projects and Donors

1) Japan's Assistance Activities:

The ongoing Power Sector Reform Advisor program will help promote governance reform at the power utility company, and the Project for Capacity Development on Energy Efficiency and Conservation supports the formulation of specific measures to improve energy efficiency. Both of these projects will contribute to the manifestation of the effects of the Program.

2) Other Donors' Assistance Activities:

The Program is co-financed with the AfDB (225 million Euro) and the AFD (75 million Euro), and monitoring of policy achievement will be conducted together with both entities.

(8) Environmental and Social Considerations/Cross-Cutting Issues/Gender Classification

1) Environmental and Social Considerations

① Category: C

② Reason for Categorization: As the Program is an ODA loan for financial assistance, it is deemed to have no negative impact on the environment, as specified in the Japan International Cooperation Agency Guidelines for Environmental and Social Considerations (issued April 2010).

2) Cross-Cutting Issues:

① Climate change: The Program falls under the category of climate change related projects (mitigation measures), as it contributes to the promotion of renewable energy and efficiency.

② Measures against infectious diseases such as AIDS/HIV: None

③ Participatory development: None

④ Disability considerations: None

3) Gender Classification:

[Not Applicable] ■GI (Gender mainstreaming needs survey/analysis project)

Reason for classification: Although gender mainstreaming needs were surveyed and confirmed for the Program, it did not lead to specific efforts that would contribute to gender quality and women's empowerment.

(9) Other Important Issues

The Program will be co-financed by the AfDB, and will contribute to the implementation of the Enhanced Private Sector Assistance for Africa Initiative (EPSA4) announced by the Government of Japan at the 7th Tokyo International Conference on African Development (TICAD 7) in 2019. In addition, implementation of the Program will cause consumers to become more conscious about energy conservation due to the increase in electricity tariffs. This is expected to promote and expand distribution for energy-saving products in Egypt, and Japanese companies have strength in the production of such products.

4. Targeted Outcomes

(1) Quantitative Effects

1) Outcomes (operation and effect indicators)

Indicator	Baseline (actual value in 2018)	Target (2021)
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Cost recovery rate for electricity charges (%)	70	100
Delinquent charges paid from EETC to NREA	No (payment not made)	Yes (payment completed)
Share of renewable energy in the power generation mix during peak load times (%)	13	20
Improvement in power generation efficiency for distribution (%)	0	10

Note: Operation and effect indicators are the same as those of the AfDB and AFD, the co-financing partners. The table above shows the main indicators.

2) Internal Rate of Return: The IRR is not calculated for programmatic loans.

(2) Qualitative Effects

Sustainable and stable power supply, mitigation of the impact of COVID-19 on economic activities.

5. Prerequisites and External Factors

(1) Preconditions: None

(2) External Factors: There will be no change in the Government of Egypt's basic policy on power sector reform. There will be no significant deterioration of the social and economic situation in Egypt.

6. Lessons Learned from Past Projects and Application of Lessons Learned to the Project

The ex-post evaluation results of the ODA loan for Pakistan "Energy Sector Reform Program (II)" (evaluation year: 2017) indicated that co-financing under a policy support framework shared among major donors contributed to the promotion of power sector reform in the Government of Pakistan. It has also been pointed out that in the aforementioned program, the combination of technical cooperation in specific areas and development policy loans provided by JICA supported the specific policy actions proposed in the policy matrix, which led to more effective policy improvements and reforms. Based on the above lessons learned, the Program will aim to achieve higher project effectiveness by combining technical cooperation to promote power sector reform.

7. Evaluation Results

The Program is consistent with the development issues and development policies of Egypt, as well as with the policies and analyses of the Government Japan and JICA. Through the provision of financial assistance, the Program will contribute to SDG 7 (ensuring access to clean and

sustainable energy), SDG 8 (inclusive and sustainable economic growth), and SDG 13 (action to combat climate change). Therefore, the need to support implementation of the Program is high.

8. Plan for Future Evaluation

(1) Indicators to be Used

As provided in 4.

(2) Next Evaluation Schedule

Ex-post evaluation in FY 2021

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